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Alfred J. Blasco

THE SERVICE CHARGE ON DEMAND DEPOSITS

By

W. GORDON JONES



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PREFACE

THIS book aims to present, in as practical a manner as possible, the much discussed matter of banking service charges on checking accounts. Inasmuch as the principal aim is to show how the service charge has worked out in actual practice among banks, it is hoped that the material included may be of some practical value to bankers, especially those who are considering the installation of the charge.

For several years past, bankers have been carrying a large number of unprofitable checking accounts on their books. Chapter I discusses this situation in general while Chapter II points out the situation in the commercial department and the reasons for these losses. Chapter III illustrates a method by which these losses can be traced and accurately determined. Chapter IV discusses the service charge as a remedy for this state of affairs and explains the various factors which enter into its installation and operation. Chapter V shows how depositors will react to the

charge and what the charge will accomplish in actual practice.

Appendix I contains some very valuable practical data obtained by the use of a questionnaire which was distributed among one hundred banks, from which seventy-one replies were received. Appendix II contains definitions of some of the terms involved as used in the book. Appendix III contains tables and charts having a bearing on the subject. Appendix IV illustrates a few of the more common forms used in the installation and operation of the charge and Appendix V contains common questions on the subject with brief answers.

I express appreciation to Mr. Horace C. Bennett, who showed great interest in this work and actively co-operated in the preparation by sending data and offering many valuable suggestions. Much of the credit for such part of this book as may be valuable is due to the many banks and other companies which so willingly gave much of the information contained herein. To them, I desire to express my appreciation and to acknowledge my obligation for their assistance.

Special acknowledgment is due to Dr. J. F. Bell, who gave me the benefit of his constructive

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criticism and aid in the preparation of the more difficult problems involved.

W. GORDON JONES.

Utica, N. Y.

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CHAPTER I

Introduction

Definition and Function of a Bank.—Banks have been defined in various ways. One author defines them as “institutions which receive deposits of money or of credit and which seek profits through the extension or sale of their own credit.”¹ Another author defines them as “institutions where deposits of money are received and paid, where credit is manufactured and extended to borrowers, and where exchange of property is facilitated.”² In addition to the extension of credit, a bank performs many other services for its customers, among which the checking account service is the outstanding, most frequently used, but yet appreciated the least by the average depositor. Thus, the functions of a bank may be summarized to include the sale of credit and services.

¹ Agger, Eugene E.—*Organized Banking*, p. 19.

² White, Horace—*Money and Banking*, p. 227. These may be supplemented by reference to any text in money and banking.

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Banking Services.—Banking institutions have been called the “Department Stores of Finance” for here are available many essential services for those in all walks of life. The small child may save his pennies in a savings account; the workman may cash his pay checks; the foreigner is provided with the required facilities for remitting funds to his native country; milady may receive advice on budget systems for economically running her home; the widow with a fortune is instructed in the principles of wise investment; the hard-pressed business man may obtain a loan which enables him to weather a depression; and the man with dependents may provide for them, when he is gone, by creating a trust fund. The word “service” fairly seeps out of the doors and windows of such an institution. Service has been and is the keynote of banking.

The value of the services mentioned above are obvious and have no direct bearing here, but there is one banking service which is used by almost every depositor, is of great value to him, and deserves the direct attention of bankers, depositors, and the general public for the simple reason that it presents an uneconomic situation to be solved only through the application of some

effective remedy for the benefit of, and justice to, all parties concerned. This is the checking account service. It cannot escape attention for it is too valuable. There are several advantages of the checking account including:

1. Cancelled checks are absolute, legal proof of payment.

2. Convenience to the depositor and enormous saving of time in making payments.

3. Makes valuable financial counsel available through contact established with bank officers.

4. Controls expenses through records.

5. To pay by check adds to the prestige of personal standing.

6. A reasonable balance provides instant ready money.

7. Keeps money safe by avoiding the danger of carrying currency.

8. Insures accuracy.

The banks are compensated for this valuable service in one way and only one way, by an ample balance in every account. This does not mean 50 per cent of accounts but all accounts. Depositors should be willing to pay for such a service by keeping a substantial balance in each

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account. Facts to be presented show that they have not done so.

A Fundamental Business Principle.—The fundamental law of business is profit. That is the purpose for which any business is maintained and the banks are no exception to the rule. They are in business to give a fair return to the stockholders and it is only just and equitable that they do so.

A bank will average perhaps \$11.50 on \$1000 per year, while it should average at least \$15 per \$1000 a year.³ Even this is a very nominal return.

Present Condition of Banks.—Reports of the Comptroller of the Currency for the past 25 years show that while the total resources of all national banks have increased 300 per cent, the net earnings for the same period have increased only 13 per cent.⁴ Earnings are not keeping pace with the increases in the other items on bank statements. Assets and deposits have been steadily swelling with earnings very much out of proportion to these other gains, as seen in the following table:

³ Driscoll, John J., Jr.—“Analysis of Accounts and the Necessity of the Service Charge,” *Proceedings of the Departmental Conferences of AIB*, June, 1928, p. 177.

⁴ *Ibid.*, p. 176.

EARNINGS AND PROFITS OF MEMBER BANKS⁵

Year	1924	1925	1926	1927
Earnings—Assets per \$1 Cap. Surplus and Undivided Prof- its	\$6.16	\$6.37	\$6.51	\$6.40
Net Earnings per \$100 earning assets	1.83	1.84	1.87	1.83
Net Profits per \$100 earning as- sets	1.31	1.40	1.37	1.35
Profits per \$100 Cap. Surplus and Undivided Profits	8.04	8.93	8.95	8.66

True profit is a percentage of the total equity of a business and not merely the original investment or capital stock of that business. Profits figured merely on capital stock are over-stated.

In a personal letter addressed to the author from Mr. Horace C. Bennett of Devlin and Bennett, Inc., Financial Advertisers, Chicago, Illinois, the latter has visualized this situation as follows:

“For some undiscoverable reason, bankers are almost universally given to the practice of stating their profits in the terms of capital stock without taking into consideration other capital investments such as surplus and undivided profits. It does not make much difference what you call invested capital. If I have a bank capitalized at \$100,000 with another \$100,000 in surplus and \$50,000 in undivided profits, I have a capital investment of \$250,000. Yet if I

⁵ Wright, Ivan—“What About the Net Profits?” *Burroughs Clearing House*, October, 1928, pp. 24, 25, 40.

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follow the practice of most banks, I shall ignore the additional \$150,000 in reporting my percentage of profit. For example, if my net profit is \$25,000, I would report it as 25 per cent when, as a matter of fact, it is only 10 per cent on my invested capital."

This means that some banks are not reporting their true profit, which, in reality is less than they claim.

Valuable service without remuneration is neither fair to any or all of the parties concerned and is not economically sound. What has been at the bottom of this trouble, for there is trouble somewhere?

The Banker's Policy in the Past.—The depositor is not to blame, however, for this state of affairs inasmuch as it has been the policy of the average banker in the past to be too conservative in regard to his profits, even reasonable ones. He has emphasized the values of the checking account and his slogan has been, "Pay by check." A checking account is very valuable and most depositors find that they cannot get along without it. These facts and valuable features should have been, and are still being emphasized correctly, but Mr. Banker forgot to consider whether the depositor could afford to keep a substantial balance or not. He sought the business

whether large or small, profitable or not. He has consequently sought this business at any cost and has paid more attention to the quantity of his accounts than their quality. Depositors opened accounts and neither they nor the bank knew whether the account was profitable or not, each supposing that mutual benefit was being derived from the business. The banker was losing money and didn't know it and the depositor was unknowingly letting someone else pay for the service he was receiving. Neither party would have approved of the situation if it had been known. Nevertheless, upon the banker alone can the blame be placed for his being too free with his service, with the result that his compensation has not been sufficient.

CHAPTER II

Unprofitable Checking Accounts

Status of Checking Accounts.—The average depositor believes that his checking account is being carried on a profitable basis, even more profitable than his savings account upon which the bank pays interest. But this is not so, for comparatively few checking accounts are paying their own way. This fact was until recently, unknown to both bankers and depositors, but a few investigations and suggestions revealed startling figures.

In 1925 the Clearing House Section of the American Bankers' Association distributed a booklet among several thousand bankers, containing a brief and simple plan for analyzing accounts. Upon applying the principles involved therein, the latter found that from 35 per cent to 60 per cent of their checking accounts were being carried at a loss.¹ This was, as near as can

¹ Simmonds, Frank W.—“Closer Interbank Relationship Imperative,” Address at the Tenth Annual Convention of District of Columbia Bankers' Association, June 7, 1928.

be determined, the initial impetus given the movement for correcting this situation. The discoveries made from this analysis tended to wake up bankers all over the country to the fact that here was a problem which needed attention and correction.

The bankers of Illinois took a very significant step in this direction and in an original investigation conducted by the bankers' association of that state about three years ago, a copy of which is reprinted in Appendix III, some relevant discoveries were made in connection with checking account balances. They found, by first determining the fact that a relatively small number of accounts carried almost all of the total deposits, that a great majority had very small balances and consequently were unprofitable.

For purposes of timely evidence and facts concerning this problem a questionnaire was distributed by the author in March 1929 among 100 banks.² Forty-nine banks reported their percentage of profitable accounts and these percentages ranged from 15 per cent to 100 per cent, but the median was 53.4 per cent.³ In almost

² See Appendix I.

³ This median may vary one or two points either way.

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every case the reporting bank had already instituted a remedy to correct this situation, which, although it had not had time to become effective, indicates that this average percentage is probably high.

It has now been pointed out that a small number of checking accounts carry most of the demand deposits and that only about half of the accounts carried are retained on a profitable basis.

Bank's Loss on Checking Accounts.—Checking accounts have been, and are unprofitable, but to what extent? How much is the average bank losing on the average checking account? The following table is based on a careful analysis of over half a million checking accounts in 800 city and country banks, the analysis showing that 64

If you have this many checking accounts	About this many will be less than \$100 Average Balance \$23.00	On the basis of 12 checks each per month, the total annual loss from these accounts is
500	320	\$ 1,996.80
1,000	640	3,993.60
3,000	1,920	11,980.80
5,000	3,200	19,968.00
10,000	6,400	39,936.00
20,000	12,800	79,872.00

per cent of all checking accounts maintain balances under \$100 with an average of \$23.50.⁴

Causes of Unprofitable Checking Accounts.—Having found that checking accounts are unprofitable and to what extent, the question naturally arises as to what are the underlying reasons for this condition and what factors are causing these losses?

In the first place, nothing will smash profits any more than increased costs and decreasing income. Such is the case here. The modern bank is equipped to give and does give excellent service to its depositors, but it is costing the bank money to give such service to its depositors and the latter should be willing to pay for that service by maintaining sufficient balances to enable the bank to pay for the cost of handling the account plus a reasonable profit. The costs committee of the Minnesota Bankers' Association recommends the following charges against the demand deposit:⁵

1. Cost of equipment.
2. Checks, passbooks, check holders, deposit slips, and other printed matter.

⁴ Devlin and Bennett, Inc.—*Advertising Data*.

⁵ McGarty, Arthur F.—“How Much Does Service Cost?” *Burroughs Clearing House*, September, 1928, pp. 14, 15, 16, 53.

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3. 90 per cent of bank space used by demand deposit activities.
4. Statements and postage for mailing statements.
5. Salaries and wages.
6. Burglary, robbery, and forgery insurance.
7. Interest on reserve money.
8. Loss in float.

Commercial department equipment includes card ledgers, signature cards, indexes and filing equipments, bookkeeping forms and machines, desks, chairs, etc., and every one of these items have increased in cost during the last few years, probably for no other reason than that they are better and enable the bank to give better service. But the bank pays the increased cost and takes a loss. Likewise, printing costs have increased and yet the banks continue to furnish checks, pass-books, check holders, and deposit slips. These conveniences are essential, and the bank is justified in furnishing them at a nominal expense but it certainly should not be requested to furnish specially printed checks with no cost to the depositor. But it does, and this contributes to a loss. Commercial department activities occupy the largest part of the floor space and thus a large amount of expense attributed to rent and taxes

must be charged against this department which maintains the checking accounts. Rent and taxes increase, causing more expense, most all of which is charged against the checking account. More loss. All checking account depositors are furnished with an accurate monthly statement. Who pays? The bank pays. Salaries and wages have been steadily increasing in harmony with higher standards of living. The bank must be protected with insurance. All these items of expense are included in the maintenance of the accounts upon the books of the bank. And it is this increased cost of maintenance that has in part caused unprofitable checking accounts.

While operating costs have been increasing, the income which the bank receives from its demand deposits has been very limited. Five per cent is about the maximum a bank can realize on the money it loans out, and when the income from an account with an average daily balance of \$100 yields only 42¢ income for a month, it can readily be seen that this small amount would hardly pay for the handling of the account.⁶ The income which a bank receives is derived very largely from its deposits for its investment in capital and surplus is almost entirely tied up in

⁶See Appendix III, Table 3.

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long term investments from which no immediate return is available. A limited income contributes in a large measure to unprofitable checking accounts.

A third reason for unprofitable checking accounts lies in the fact that some depositors draw numerous checks against their accounts. A dormant account is obviously an inexpensive one to handle while an account showing great activity is a costly one.⁷ More checks, check books, statements, work involved in maintaining the records, and time of clerks is needed on these over-active accounts. Depositors should be limited in the number of checks which they are allowed to draw unless they pay for the increased cost involved.

As was pointed out in the preceding chapter, the banker's policy has been more business at any cost, quantity instead of quality, and the challenge to the depositor to pay by check whether he can afford to maintain a substantial balance or not. Out of this policy has grown four wrong ideas among low balance checking depositors:⁸

1. Do not appreciate or know all the values of checking service.

⁷ See Table on Page 18.

⁸ Devlin and Bennett, Inc.—*What About the Service Charge?*
A booklet.

2. Do not realize the value of an adequate balance.
3. Believe all checking accounts are profitable to banks regardless of size.
4. Feel they are conferring a favor on the banks.

Bankers in the past have fairly begged for checking accounts regardless of the quality of the account and naturally these ideas would develop among depositors for they were not educated to the facts. The bankers themselves in many cases were ignorant of the losses they were incurring, but the depositors cannot be blamed for it is through the bank only that they are educated to banking costs and practices. Therefore, the bankers themselves have been largely to blame for the large number of unprofitable checking accounts.

Some banks make a practice of paying interest on demand deposits without considering whether they can afford to do so or not. This is a contributing cause of unprofitable checking accounts.

According to national banking laws under the Federal Reserve Act, banks are required to keep a certain per centage of their deposits in reserve for an emergency. This deduction from the amount deposited is necessarily of an unearning

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character and reduces the balance subject to earnings. Against the demand deposits these reserve requirements are:

- 7% Country Banks
- 10% Reserve City Banks
- 13% Central Reserve City Banks

according to the size of the city in which the bank is located, while usually most banks maintain a little in excess of the requirement for safety. Against the time deposit a reserve of 3 per cent is required and although the bank pays interest on these deposits, its balance subject to earnings is not so materially reduced as in the case of the demand deposit.

An additional cause for unprofitable checking accounts is float or uncollected funds. As checks are deposited an immediate credit is given to the depositor on the books of the bank, but the actual funds are not collected for some time, depending on the location of the bank upon which the check is drawn. The bank consequently loses the interest on this money for the time involved in collecting it. The Federal Reserve Time Schedule, showing when the proceeds of items will become available, is reproduced in Appendix III.

Two causes of unprofitable checking accounts arising out of float are the practices of allowing

interest to be paid on uncollected items, and permitting depositors to draw against uncollected funds.

"The bank cannot earn money on balances which exist only as bookkeeping records, and since the bank must have possession of funds before it can loan or invest them, logically it cannot pay interest on uncollected balances." ⁹

A depositor drawing against uncollected balances is merely receiving a loan from the bank.

"The bank maintains its reserve on the ledger balance, protects the depositors' interests, does the work of collecting, and yet there is no actual money in hand by which it may obtain its just earnings. Cases are of record where the float has so added to costs of service, that the banks handling the business actually suffered a loss on accounts that kept the average daily ledger balances approximating \$10,000." ¹⁰

An indirect cause for unprofitable checking accounts is the increasing use of checks as a means of making payments. In response to the widespread advertising to "pay by check," most every one makes payments in this way regardless of whether a substantial balance may or can be maintained or not. Money is changing hands at a greater rate than ever before. In 1927 Ameri-

⁹ American Bankers' Association—*Does the Account Pay?* p. 5.

¹⁰ Devlin and Bennett, Inc.—*Uncollected Balances*, p. 6.

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cans used seven billion checks, seven hundred million of which were supplied by one company which claims that present orders indicate an increase.¹¹ More checks mean more activity; more activity means more expense in handling the accounts; and more expense means more unprofitable checking accounts.

Finally, the amount of the balance is very important and unprofitable checking accounts are caused in the main, by this one weakness, small balances. Raise the balances and that fact alone will automatically decrease the number of unprofitable accounts. As the balances increase, the losses decrease.

No. checks issued per month	Annual Earnings and Losses from an Average Daily Balance of			
	\$50	\$75	\$100	\$150
2	4.22	2.89	1.57	1.01* ¹²
4	4.72	3.39	2.07	.51*
6	5.22	3.89	2.57	.01*
8	5.72	4.39	3.07	.49
12	6.72	5.39	4.07	1.49
16	7.72	6.39	5.07	2.49

The situation is merely free service, service with no return. Even with a balance of \$150 a

¹¹ Todd, Walter—"Use of Checks Increasing"—*The Bankers Magazine*, September, 1928, p. 484.

¹² The starred figures represent profits while the rest represent losses.

bank cannot earn but just barely enough to pay for maintaining the account. From investigations and figures which have already been pointed out, this weakness seems to be the case with a majority of checking accounts, and this is the basic and most evident cause of unprofitable checking accounts. The higher the balance, the more money a bank has to work with, the higher its balance subject to earnings will be, and a corresponding decrease in loss of handling the account will be the result.

However, this does not necessarily mean that an account with a large balance is always profitable, for float or some other cause of unprofitable checking accounts may be eating up the profits. Checking accounts that are unprofitable naturally divide themselves into two classes, those small and usually personal accounts, and those larger accounts, usually maintained by a business house.

An Uneconomic Situation.—It has been pointed out that a majority of checking accounts are unprofitable and the reasons for that condition have likewise been indicated, but what does this mean? It means that a majority of depositors are not paying for what they get and that the bank is taking a loss or relying on its

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profitable accounts, maintained by other depositors, to pay for the losses incurred in giving the same service to those who do not appreciate the value of the service they are getting, by maintaining a sufficient balance or paying the loss incurred. Service for nothing, service being paid for by someone else, whichever way you look at the matter, is not economically sound or fair to the bank, the depositors, or the general public.

"The significant and distinctive feature of banking service in the United States is the universal deposit and check system of making payments. The characteristic tendency of the banker, stimulated by keen and wholesome competition, to offer banking facilities without limitation, has reached a critical point. Because of greatly increased overhead costs, it is no longer economically possible to ignore the distinction between the depositor who uses the check to avail himself of accumulated credits and the depositor who gives no thought to his obligation to the bank, other than to keep a few dollars on deposit, usually (but not always) sufficient to meet the checks he draws.¹³

Having stated the situation as it exists, and pointed out the place where the greatest weakness is, and the causes for it, the next steps are to indicate a method by which the amount of the loss can be accurately determined, to suggest a

¹³ Wolfe, C. Howard—President of Clearing House Section of A. B. A.

remedy for it, and to show what this remedy has already accomplished and will accomplish in actual use. The problem is to correct an uneconomic situation.

CHAPTER III

Determining the Unprofitable Account

Knowledge of Costs.—The first thing to do in connection with this problem is to determine the operating costs or expenses incurred in the handling of a checking account. Analysis is the keynote of this procedure. The word “analysis” may to some people suggest complication and difficulty, but it is really a simple matter.

A bank may best proceed by setting up a number of schedules: ¹

Schedule I.—This is known as the Division of Expenses and, as the name implies, contains a list of all the expenses which a bank incurs, the total amount of each, and the distribution to each department. The purpose of this is to localize all expenses and charge to each department the amount of the total expense which is directly attributable to the maintenance of that department. For instance, the item “rent” would be distributed among the several departments in the proportion which the space occupied by each

¹Based on “Report on Operating Costs”—Recommended by Driscoll, Yergens and Company of Philadelphia, Pa., accountants.

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bears to the total floor space. After each expense has been so distributed, the net result is the total expense incurred by each department. The one with which we are concerned is the commercial department.

Schedule II.—Having determined the total expense of the commercial department, the next logical step is to divide this expense into three elements which make up commercial department expense. These elements are activity, size, and maintenance. The breaking up of the expense items into these component parts is the purpose of this schedule.

Activity cost is that attributed to the handling of the checks including cost of handling in and out items, supplies, teller's, clerk's and bookkeeper's salaries, printing, stationery, advertising, etc., and depends on the number of items handled. This is done by dividing the total activity expenses by the total number of items handled. This results in a per item cost of about 4¢, which may or may not vary among different banks. Some banks find that items deposited cost less than those paid and differentiate between these two. Checks on the bank itself concerned are the most expensive items to handle due to the additional bookkeeping, filing, etc., involved.

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Size cost is based on the amount on deposit in a specific account and is that portion of the total commercial department expense, which the amount on deposit bears to the total commercial deposits. Thus, to find the size cost, the total size expenses are divided by the average deposits, resulting in an average cost of about \$4.63 per \$1000 per year or about 38¢ per \$1000 per month. This, of course, will vary among different banks.

Maintenance cost is the cost of maintaining the account on the books of the bank and is the same for every account regardless of activity or size. This is found by dividing the total maintenance expenses by the average number of accounts and results in an average maintenance cost of about \$2.64 per account per year or about 22¢ per account per month. This, too, will vary among different banks depending on the figures used by each.

To summarize, these three costs may be indicated by formula as follows:

$$\begin{aligned}\text{Activity Cost} &= \frac{\text{Total activity expenses}}{\text{Number of items handled}} \\ \text{Size Cost} &= \frac{\text{Total size expenses}}{\text{Average Deposits}} \\ \text{Maintenance Cost} &= \frac{\text{Total maintenance expenses}}{\text{Average number of accounts}}\end{aligned}$$

It must be kept in mind that it is impossible to accurately set any figures for these costs as they depend entirely on the condition of each bank. By the simple process of analysis indicated above, any bank, regardless of size, may determine these costs to advantage. Each one may arrive at different figures, proceed in a slightly different manner, and use other names for the cost, but the principles involved, as outlined above, are the same. The result is an accurate knowledge of what it costs to maintain the checking accounts.

The tables on page 26 are based on a hypothetical bank with 650 checking accounts. All of the items closely conform to the proportions that would be found in any bank of this size. Experience has shown that these same ratios hold true in the average commercial bank regardless of size.

Schedule III.—Knowing the costs the next step is to determine the average income on the funds available for investment. This schedule may be called "Funds Invested and Income Earned" and contains a description, the amount, the income, and the rate per annum of each investment. The average total income is then determined, from which is deducted the invest-

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DISTRIBUTION OF EXPENSE ACCORDING TO DIVISION OF BANK ^a

Expense Accounts	Totals	Checking Accounts	Saving Acct. Cths. of Dept.	Loans and Investment	Misc. Div.
Advertising ...	547	350	150	...	47
Building	543	275	125	103	40
Insurance	1,880	943	342	480	115
Salaries	7,873	3,150	700	3,813	210
Stationery	900	516	197	172	15
Taxes	2,313	810	460	1,006	37
Misc.	224	93	8	120	3
Totals	14,280	6,137	1,982	5,694	467

DISTRIBUTION OF EXPENSE OF CHECKING ACCOUNT DEPARTMENT ^a

Expense Accounts	Totals	No. of Accts.	Activity of Ac-counts	Overhead
Advertising	350	350
Building, etc.....	275	25	75	175
Insurance, etc.....	943	112	278	553
Salaries	3,150	690	2,060	400
Stationery, etc....	516	108	317	191
Taxes	810	200	200	410
Misc.	93	13	40	40
Totals	6,137	1,148	2,870	2,119

ment cost. This gives the net return on average investments and averages about 5 per cent. In formula form, this may be expressed as:

$$\frac{\text{Net Income Earned on Investments}}{\text{Average Funds Invested}} = \text{Rate per annum}$$

^a Devlin and Bennett, Inc.—*What About the Service Charge?*

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Analysis of Accounts.³—With this knowledge of costs and the average income earned, a bank is in possession of the figures necessary to determine to what extent an account is unprofitable, by the process of what is known as the analysis of an account.

The first step in this procedure is to find the average daily balance of the account under analysis. This is done by taking the total of the balances for each day of a month and dividing by the number of days in the month.⁴ From this amount there are deducted two items, float and reserve. The former is called the daily average in process of collection, represents the daily average of uncollected funds, and is determined by the

³ Monthly basis.

⁴ Each day the deposits that you have made and the checks which have been presented for payment are recorded on your account at your bank. Suppose you had \$100 remaining from the day before—then you deposit \$50—and that checks totaling \$23 are presented that same day. This would make total credits of \$150.—total debits for \$23. Your balance at the close of the day would, therefore, be \$127. This is known as the daily ledger balance. To compute the average daily balance, the bank simply totals all of the daily ledger balances and divides by number of days in the month. The result is the average daily balance for that month.

"Inasmuch as there is some difference of time between the drawing of the check and its payment by the bank, there would be some small difference between the bank's recording of your average daily balance, and the amount that you would reach by figuring from your check book stubs." Devlin and Bennett, Inc.

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use of what is known as the transit float account.⁵ The reserve is found by taking the per centage, used by the bank in question depending on its location and requirements, of the average daily balance. The net result of these two deductions gives the average balance subject to earnings. Then, the income on this available balance is figured and as we have seen, averages about 5 per cent. Finally, the costs, including activity, size, maintenance, and other miscellaneous expenses such as special checks and books are figured and the total cost determined. If this cost is in excess of the income earned on the available balance, the account shows a loss. This procedure may be more clearly explained and understood in account form as follows: ⁶

Name.....John Doe.....
Month of....February.....

ANALYSIS OF ACCOUNT

Average daily balance.....	896....
Daily average in process of collection.....	340....
12% reserve in vault and with bank.....	107.....447....
Average balance subject to earnings.....	449....

Income

Interest on available balance at 5%...449.....	1.87
--	------

⁵ See Appendix III, Table 5.

⁶ Actual account with fictitious name. Form and procedure through courtesy of Oneida National Bank of Utica, N. Y.

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Cost

Number of checks deposited @ .02½.....	144.....	3.60
Number of checks paid @ .04.....	69.....	2.76
Special check books furnished.....		22

Overhead

For size \$.890. @ .31 per M per mo.....	26....
For maintenance @ .27 per mo.....	27 7.11
	Profit.....
	LOSS..5.24

Remarks

Accounts may be unprofitable for any one of the reasons stated in the preceding chapter, but the purpose and result of analysis is to show clearly where the cause for the loss lies and how much that loss is.⁷

Analysis Systems.—In using this method of determining whether an account is unprofitable or not, it is not necessary to analyze every account in the bank for the law of averages applies and the banker, having analyzed a representative group of accounts, can readily determine upon what basis the account must be kept in order to be profitable in so far as the amount of the balance is concerned.

The distinction between the two general types of unprofitable accounts must be kept in mind, small accounts, unprofitable because of insuffi-

⁷ See Appendix III, Analysis of Accounts.

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cient balance, and the larger accounts, unprofitable for some other reason.

In analyzing a small number of small checking accounts, the banker soon knows just about what the minimum balance should be to put the account on a profitable basis. He can thus set a fixed amount below which the small accounts cannot fall without being a loss to the bank.

As far as the larger accounts are concerned, these are analyzed individually for they may be unprofitable for one or more of various reasons such as float or high maintenance or activity cost.

It has already been shown that the majority of accounts are small and keeping in mind the relative simplicity of the procedure and the fact that few accounts have to be analyzed as the law of averages applies, it is logical to assume the value of analysis.

What Analysis Shows.—As a simple, sound, successful, inexpensive step in the direction of correcting the uneconomic situation at hand, analysis has great value for four reasons:

(a) Shows that a bank can lose on big accounts as well as small ones.

(b) Shows the reasons for and the extent of the losses on checking accounts.

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(c) Shows the banker how to fix a basis for service charges.

(d) Shows the depositor why a service charge is necessary.

CHAPTER IV

Installation and Operation of the Service Charge

What Is a Service Charge?—Any service charge is, as the name implies, a charge made, by an institution or person performing some particular service, against the beneficiary of that service. In practice, it means nothing more or less than paying for what you get. Banking service charges are made for various services which these institutions perform for their customers, but the one with which we are concerned here is the service charge on demand deposits or checking accounts. The service charge on demand deposits "is and should be regarded as a payment which the depositor willingly makes as partial payment for the service which the bank renders in providing checking account service for depositors whose average balances do not exceed \$100"¹ or some other minimum balance fixed by analysis in the bank concerned. This definition

¹ Bennett, Horace C.—"Is Your Stop Loss Charge Satisfactory?" Published by Devlin and Bennett, Inc., and reprinted from *Illinois Bankers' Association Bulletin*.

provides only for a charge on small accounts, but the charge may also apply to depositors whose accounts, although above the required balance, are unprofitable for some other reason.

The Purpose of a Service Charge.—The purpose of the charge is, of course, to stop some of the losses incurred in handling checking accounts. It is a remedy for an uneconomic situation, by which everyone pays for what he gets. Keeping in mind the distinction between the small and large accounts, the service charge on the latter class is an end in itself, but on the small accounts, it is merely a means to an end and that end is increased balances. In other words, the service charge may have for its purpose payment for services rendered or may be used merely as a penalty or a correcting influence. In either case, the ultimate aims of this remedy are the placing of checking account service on a sound economic basis and the stoppage of losses. Through the service charge, the depositor pays for service rendered and does this by either keeping a substantial balance or by the payment of a fee.

Installing the Service Charge.—The first step in the installation of a service charge is to determine the cost of handling the accounts including a knowledge of costs applicable to the

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demand deposit and an analysis of the accounts as outlined in the preceding chapter. This is essential for determining upon what basis the charge is to be made and for a clear explanation to the depositor as to the reasons for the charge.

With this information a bank can proceed to set an average daily balance below which an account cannot drop without being charged, which is the primary consideration for the small accounts. Thus, upon analyzing several hundred accounts a bank may, upon the application of the law of averages, conclude that an account to be on a profitable basis must have an average balance of \$50, \$100 or more as the case might be. When the income from a balance certain, from which proper deductions for float and reserve have been made, just equals the sum of the costs of handling the account, that amount certainly should be the required average daily balance.² This average daily balance is the basis

²(a) Average Balance \$100

	Income
	\$.37
<i>Cost Description</i>	
Size Cost	\$.04
Maintenance Cost22
3 Items @ .034.....	.10
	<hr/>
	\$.36

(b) Average Balance \$150

	Income
	\$.55
<i>Cost Description</i>	
Size Cost	\$.06
Maintenance Cost22
8 Items @ .034.....	.27
	<hr/>
	\$.55

upon which the service charge on small checking accounts is made.

But in fixing a service charge on small accounts, in addition to the basic consideration of balance in the account, the factor of activity must also be considered. For any additional items paid, to the number allowable in order to just break even on an account, a charge is made although the balance may be sufficient.

Upon the bases of balance and activity, the charge is made and this too, will vary between banks, depending upon size, local conditions, etc. These charges will range from 50¢ upward per month.³ For example, a service charge complete, might be stated as \$1 per month when the average daily balance for the month does not equal \$100, allowing 15 checks to be drawn.⁴ This would be a just and equitable charge for a bank with resources of about twenty million dollars in a city of about one hundred thousand people. This charge would be made in either of two cases, that the average balance drops below \$100 or

* See Appendix I, Question VIII.

* Graduated scale applies.

Thus—On balance of \$200—30 checks allowed

On balance of \$300—45 checks allowed
and so on, 15 checks per \$100 balance.

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that more than 15 checks are drawn during the month.

It is very important to note in connection with the service charge on small checking accounts that they can be given mass treatment and a flat charge adopted, which applies to all accounts. This is not true when considering the larger accounts to which individual treatment must be given. Each of these accounts must be analyzed as illustrated in the preceding chapter and the loss shown is the service charge which will be different for every account. For instance, in the case of the account under analysis, illustrated in the preceding chapter, the service charge for the month would be the loss as shown.

Determining the cost of handling the accounts, the required average daily balance, and the charge to be made on all accounts which are unprofitable, as indicated above, is the initial step in installing the charge.

Co-operation of Other Banks.—It is advisable, although not absolutely essential, to secure, if possible, the co-operation of the other banks in the same city or county. This may be done through the execution of county or clearing house agreements.⁵ However if this co-operation can-

⁵ See Appendix IV, Clearing House Agreement.

not be effected, it is possible for a bank to install the service charge without it. But there are advantages in co-operation including: ⁶

- (a) Concerted action strengthens plan.
- (b) Divides the burden of educating public.
- (c) Increases the spirit of co-operation among banks.
- (d) Relieves any one bank of the responsibility of introducing the charge.

Clearing house rules are enforceable among banks and should be strictly adhered to in connection with service charges.

"Four banks in Janesville, Wisconsin, now using the service charge were required to put up a \$500 bond for strict adherence to rules of the clearing house association." ⁷

Education.—The service charge is a proposition which is more or less of a repulsive nature upon the face of it and it is justified and accepted by all concerned only when fully understood. Therefore, it becomes the problem of the bank installing the charge to educate officers, directors, employees, depositors, and the general

⁶ A. B. A.—"The Service Charge—A Plan for its Installation and Operation."

⁷ Personal letter—President, First National Bank, Janesville, Wisconsin.

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public as to the reasons for the charge and the economic soundness of it.

The educational work involved may be undertaken by the bank's own personnel if adequate, but it is advisable to hire outside help if such is not the case. In case a bank cannot handle the work itself there are financial advertisers available who make a specialty of this type of work.

The work itself begins within the bank and consists of selling the proposition to the officers, directors, and employees. This may be accomplished through personnel meetings, distribution of booklets, and discussions, all of which emphasize the service charge. All who come in contact with customers should be able to meet any objections that may arise. Of course, the officers or the officer in charge of service charges will naturally more fully understand the case at hand and although employees may handle customers as best they can, when the employee finds that he cannot meet the customer's objections adequately, or finds that the customer is not fully convinced, the best thing to do is to request an officer's aid in the matter.⁸

Educating the depositor must be given care-

⁸ See Appendix IV, Request for officer's help.

ful consideration. There are several means by which this may be done including:

- (a) Personal letters.⁹
- (b) Circular letters.
- (c) Personal interviews.
- (d) Newspaper advertising.
- (e) Booklets.
- (f) Announcement cards.¹⁰

The methods used depend entirely on local conditions and each bank can best determine for itself what means of education it should use to best advantage. However, a questionnaire, distributed among banks who have already installed the service charge reveals significant information in connection with the problem of education, in which it was found that 91.5 per cent of those submitting answers consider educational work concerning the service charge advisable, 40.8 per cent would consider preparing educational work themselves, 58 per cent would employ outside help, and 90.1 per cent think it worth while to train employees to handle any objections that may arise.¹¹

⁹ See Appendix IV, Personal letter.

¹⁰ See Appendix IV, Announcement card.

¹¹ See Appendix I, Questions III, IV, V, VI, and VII.

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Cost of Installation.—The cost of installation will vary, of course, among banks, depending upon the methods used, but in any case the cost involved will be small in proportion to the gains derived from the charge. One bank in Illinois found that the complete cost of installation was paid in full by the first three months' service charges.

Operation of the Service Charge.—The service charge, when put into operation, will produce the desired results, as will be explained in the next chapter, but there are several things to be kept in mind.

In the first place, it must be remembered that the charge is a problem in salesmanship and convincing those affected by it that it is a fair proposition should never be neglected. If the depositor does not understand why his account should be charged through the medium of letters or advertising, he should be invited to call at the bank where someone will go over his account with him and explain why it is unprofitable. If this is done, he will become convinced that he should pay for the service he is getting and that it is only fair that he should do so. Checking account service and its values should be emphasized in addition to the values of a substantial balance.

Secondly, it is essential that the bank maintain good-will in every case, for that is among its most valuable assets. In this connection arises the question as to whether general broadcasting of the subject of service charges is advisable, in which case many who would not be affected by the charge itself are included. Would it not be better to merely notify the unprofitable customers through letter or personal interview and thus bring the subject to the attention of only those directly concerned? That is a problem for each bank to decide for itself but, in any case, educate and convince the customer to the charge. It should not be forced upon him and he should be given every possible benefit of any doubt.

A most important consideration is the time to put the charge into effect. It should not be slapped on with no notice whatever, but should be preceded by an extended period of education in which the depositors have a chance to understand and will not have a charge slip thrown in their faces on five minutes' notice. This period may be from one to three months depending upon local conditions. A service charge should be announced considerably in advance of the time that it is to take effect.

In determining the amount and basis of the

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charge, in order to avoid a lot of unnecessary questions and misunderstanding on the part of depositors in the future, it should be sufficient, that is, high enough, when first installed. It was found in a questionnaire that 35 per cent of banks who had already installed the charge would raise either or both the amount and basis of the charge if doing it over again.¹² A service charge should be sufficient to start with and thus avoid raising it later on when found to be insufficient.

No accounts should be lost if it is in any way possible to maintain them even though they merely pay their keep, as future possibilities of appreciation and valuable connections must be considered. In this connection it is important to keep in mind the character of the depositor and how much his business is worth to the bank. However, some accounts are better lost than maintained for they are not profitable and never will be.

"We do not want to lose a single account we have—small or large—if we can possibly have them on at least a cost basis. We merely want them to pay for the cost of handling their own business. Our theory has been that the small accounts would some day grow to be large ones and

¹² See Appendix I, Question IX.

therefore we are willing to handle them at a cost, not a profit, with that end in view.”¹³

This means that although the ultimate aim of the service charge is increased balances and profitable accounts, payment of the charge itself will be accepted in lieu of losing the account although the balance is still not profitable. The charge merely pays for the keeping of the account with no reasonable profit.

In case a depositor cannot afford to maintain a profitable checking account, it may be advisable to advocate a transfer to a savings account until such time as a substantial checking balance can be carried.

Where two depositors in the same family, especially in the case of man and wife, are maintaining small accounts, payment of the charge may be avoided by suggesting the use of the joint account which will in usual cases become profitable because of the union of the two balances to a point above the required minimum.

The matter of making exceptions has been found to be a point of great controversy among the banks which have already installed the service charge. Some claim that they make absolutely

¹³ A. B. A.—“A Conversation Between a Depositor and a Banker Regarding Service Charges on Small Checking Accounts.”

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no exceptions while others say that exceptions are necessary.¹⁴ If any definite exemptions are to be made, as in the case of employees, religious, fraternal, and charitable organizations, these should be fixed prior to the installation of the charge and strictly adhered to.¹⁵ The matter of making exceptions is directly related to maintaining goodwill and, as this is a primary consideration, exceptions may be made but only for a good reason involving some other connection with the bank, which is profitable. However, a bank should not grant any unreasonable demands.

Service charges may advantageously be applied in any bank, regardless of size or whether the co-operation of other banks can be secured or not.

“Our experience justifies the belief that there is no bank too small for the service charge and that while it is more satisfactorily enforced when all of the banks of the town agree to the rule, yet any bank can successfully enforce it without the co-operation of its competitors. This is true because of the fact that the more accounts of the character of those that are affected by the service charge the bank loses, the better it is for the bank and the poorer the

¹⁴ See Appendix I, Question I.

¹⁵ See Appendix I, Question X.

competing banks will be for accepting that class of business without applying the service charge.”¹⁶

In operating the service charge, a bank should keep in mind the distinction between the small and large accounts and the place to start the charge is with the low balance depositors. After the charge on the small accounts has been in effect a reasonable time, then the larger accounts may be analyzed and subjected to the charge.

“The reason we have concentrated on low balance depositors is because it offers the quickest source of additional revenue at the lowest cost to the bank, and because the solution of the problem is comparatively simple once you have corrected the basic misunderstandings which most depositors have regarding checking account service.”¹⁷

A bank, in the entire operation must be guided by local conditions and hard and fast rules are impossible to set. The only hindrance to its successful operation is the competition for new accounts and the advertisement by non-charging banks to that effect, but it has been found that

¹⁶ Stephens, Dan V.—“The Service Charge Experiences of a Small Bank,” A. B. A. Booklet, *The Service Charge on Unprofitable Checking Accounts. A Plan for its Installation and Operation*.

¹⁷ Personal letter from Mr. Horace C. Bennett of Devlin and Bennett, Inc.

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the latter class will lose in the long run by accepting unprofitable accounts.

To summarize, we have now considered the situation with regard to unprofitable checking accounts and the underlying causes, have determined upon a method by which unprofitable accounts may be located and the amount of the loss determined, and have suggested the service charge as a remedy by explaining its installation and operation. Our next and final step is to see how the service charge has worked in actual practice, the results obtained by the use of it, and its advantages to the bank, the depositors, and the general public.

CHAPTER V

What a Service Charge Will Accomplish

Effect of a Service Charge.—Once a service charge is installed, the depositors will react in one of several ways:

- (a) Willingly pay the charge.
- (b) Increase balances.
- (c) Withdraw accounts.
- (d) Transfer to a savings account.
- (e) Consolidate with other accounts.

The service charge, having two principal purposes, either payment for services rendered or a correcting influence, has been favorably received wherever it has been put into practice in the correct manner. The class who willingly pay the charge comprises those depositors who maintain the business or larger accounts, and realizing the value of the service rendered, pay for it without objection in the majority of cases. This class may also include a few depositors carrying small accounts, who, for some good reason cannot afford to maintain the required balance and would rather pay the charge and of course, re-

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tain the benefits of checking account service. Those who increase their balances are fulfilling the ultimate end of the charge on small accounts and reaping the benefits of a larger balance by so doing. Those who withdraw their accounts because of the charge are few in number and are unreasonable to the extent that they will not pay for what they get and would rather have free service than a strong bank. Some depositors will transfer their account to the savings department to avoid payment of the charge and usually discover later that they cannot get along without checking service and transfer back, either paying the charge or increasing their balances to the required amount. A few are justified in transferring to a savings account in cases where they cannot afford to pay for checking service. By so doing, they make their accounts less expensive for the bank to handle and continue their banking connection until such time as they can afford to maintain a checking account. Very often accounts of the same family or some other personal or business connection are consolidated into a joint account which is profitable to the bank because of the increased balance and avoids payment of the charge on two or more smaller accounts.

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A study of the immediate reaction of one hundred low account depositors revealed the following figures: ¹

9—Consolidate with other accounts.

Transfer to savings.

Normal closings.

11—Close because of charge—average balance, \$15.47.

32—Build balances and escape charge.

48—Pay the charge.

According to these figures the majority pay the charge, but it must be remembered that this is an immediate reaction and after the charge has been in effect a reasonable time a large percentage will increase their balances, which is the desired end. The collection of service charges is greater the first few months of its operation. As time goes on, these collections decrease as depositors increase their balances to avoid payment of the charge, making the ultimate end of the charge on small accounts a realization of a profit from a substantial balance.

However, no matter what may happen in individual cases, the application of the service charge as a whole meets with practically few objections. In itself, it is economically sound, reasonable, fair, and just. Service charges have for many

¹ Devlin and Bennett, Inc.—Booklet, *What About the Service Charge?*

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years been a common practice with some of the larger banks, but it has only recently been adopted by most of the smaller or country banks where the emphasis is shifting from the number of accounts to quality of accounts.

Any fear of its not "going over" with the depositors has been dispelled by proper installation, education, and the maintenance of goodwill. It has the endorsement of labor unions. Dispatches received indicate that the South Carolina Senate has unanimously rejected the bill to prohibit the service charge and in a recent decision of the Mississippi Supreme Court the charge was given a clean bill of health as to its legality. All these observations are of little value unless we determine how the banks themselves feel about the charge and what effect it has had on their business. The experiences of a number of banks who have recently installed the charge are as follows:

Bank 1.—We are well pleased with it. Our deposits did not decrease and the service charge collected monthly is gradually getting smaller, showing the results desired—building up of deposits with profitable balances.

Bank 2.—The rigid application of an *adequate* service charge is very necessary if banks are to

remain prosperous and earn a fair and reasonable dividend—but *only* as a means to educate people to maintain balances commensurate with the volume of their business.

Bank 3.—Since adopting the service charge several years ago, we have recently changed our charge from 50¢ to \$1 on balances below \$50. We recommend that if any banks are considering a service charge they make it plenty high to start with so that no changes would have to be made in the future as it eliminates a lot of unnecessary questions raised by depositors.

Bank 4.—We have found that the charge will raise balances. We recommend education through personal interview only, and exceptions in case of other profitable connections.

Bank 5.—See table on page 52.

Bank 6.—Our printed matter with reference to the service charge was sent out to 1650 of our customers. I would estimate that about 150 of the above customers carried an account generally in excess of the \$100 daily average, leaving 1500 accounts usually below the \$100 daily average.

700 accounts are now paying the service charge
300 accounts have increased their balances
500 accounts have been closed

Of this 500, probably one-half were dormant accounts having only a very small balance. Of the remainder quite a number were closed through consolidation with other accounts, that is, where both husband and wife were carrying personal accounts they were consolidated into one. Quite a number of accounts were closed because the people thought it would be impossible for them to carry a daily average of anywhere near \$100 and decided to do without a checking account. Very few, if any, of the accounts were taken to competing banks. We are very well pleased with the results and our customers, generally, appreciate the fairness of the arrangement. It has in no way decreased the amount of our total deposits.

Bank 7.—We are getting wonderful results. Very little trouble. Bankers are very much sold on this charge. Public seems satisfied.

Bank 8.—We put on an educational program and we are well pleased with the results.

Bank 9.—40 per cent of the accounts affected brought balances up to the requirement in the *first three months*.

Bank 10.—Number of checking accounts reduced in two years about 25 per cent to 30 per cent, but balances of those retained were from

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70 per cent to 75 per cent larger than former totals.

Bank 11.—In treating 1050 unprofitable accounts, at the end of 60 days we had the following results:

Number of accounts charged service charge.....	540
Exempt on account of having savings account of \$300 or over	85
Accounts closed	133
Accounts with balances increased	206
Accounts remaining inactive	76
	<hr/>
	1050

We have made the exception among the local banks of charging on checking accounts when the parties carried a savings account in *their* name of \$300 or more. We also exempted people who had accounts of \$100 or less on which no checks have been drawn. Our service charge, through the clearing house, has been conducted for about five months. We have now lost about four hundred of the original 1050 accounts, as one of our local banks left the clearing house and handled small unprofitable accounts without charge. Of the 206 accounts who increased their balances, the average balance was \$379 when previously they carried less than \$100.

Bank 12.—Where charge is uniformly adopted in a community, many unprofitable accounts are

shifted from one bank to another and on a proper paying basis at the new location. Net result—few lost and all better.

Bank 13.—Reactions have been pleasing to such an extent that we regret we did not inaugurate this system years ago.

Bank 14.—Service charge went into effect April 1, 1928. At that time accounts under \$100 were 52.8 per cent of total accounts. Accounts \$100 to \$300 were 21 per cent of total accounts. February, 1929, accounts under \$100 reduced to 45 per cent—\$100 to \$300 increased to 26 per cent. Service charge generally accepted as justified.

Bank 15.—Very satisfactory arrangement. Lost some accounts, but our average charge is on 200 accounts, a revenue to the bank of \$100 a month, besides increased balances and savings on checks and stationery. The small accounts were the biggest users of checks.

Bank 16.—All banks (nearly) in this district worked together in putting it across. Arrangement very satisfactory. Charge is against about 20 per cent of all commercial accounts.

Bank 17.—While we closed about 700 small commercial accounts during the first half of 1928, our commercial balances this date are about

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\$100,000 higher than they were a year ago. The total of the monthly charges has dropped from 402 for the first month to 261 for January, 1929.

Bank 18.—Decrease in accounts and cost of operating and an increase in deposits.

Bank 19.—Have larger profits for the bank.

Bank 20.—Our bank lost over 4000 accounts, but gained in deposits. All bankers well pleased with the service charge and would not go back to the old way.

Bank 21.—We consider our experience absolutely satisfactory. We did a thorough job of educating both the public and our internal organization as to the necessity and the equity of the charge. We used direct mail, newspapers, window and lobby displays. It was a joint campaign of four clearing house banks and trust companies. Results: a shrinkage in the number of accounts (all of them heavily unprofitable); an increase in aggregate deposits; a building up of individual deposits; an increase in revenue (from the fees); a better appreciation of the worth of bank service on the part of the customer. We have created in the average depositor's mind an appreciation of the value of a checking account and other bank services. We have also been able to reduce our salary expenses somewhat. We

give better service now to our checking account customers.

Bank 22.—In the movement to impose a service charge, all the banks in the clearing house joined and engaged a firm of financial advertisers in Chicago to conduct the campaign. The firm held several meetings with the officers and employees of the banks and gave full instructions concerning the new system. It also provided literature to be mailed to the bank's customers and provided "copy" for advertisements in the newspapers. As a result of the measures of preparedness, the innovation was effected without friction. Naturally all the banks lost some customers, but almost without exception these were of the non-profitable class and at the close of the first month the sum total of the service charges far more than compensated for the closed accounts. One very gratifying feature of this system is reduction in overdrafts. Many who closed checking accounts opened interest-bearing accounts. The adoption of a service charge by the banks imposes no hardship because the security and convenience afforded by a checking account easily is worth the small fee that is exacted. In my opinion, banks and customers alike, are satis-

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fied that the service charge is warranted and worth while.

Bank 23.—We lost many small accounts. These involved much labor because they deposited small amounts each day and immediately drew checks against them. Our checking account total deposits grew larger due to the increased balances and we did not need the services of three or four employees—one teller, two bookkeepers, and one clerk.

Bank 24.—Results are all that could be desired in spite of the fact that our plan was anything but perfect. In 30 per cent of the accounts treated we found increased balances.

Bank 25.—Our experience has been that we lost no worth-while business either from the standpoint of balances or goodwill and that, in about 75 per cent of the cases, our customers have raised their balances to the required amount.

Bank 26.—The service charge is working very satisfactorily. When it was first started we lost approximately 600 personal checking accounts. However, they only averaged a balance of about \$30 per account so the loss from the standpoint of revenue was not startling. We lost very few business accounts owing to the fact that we so

thoroughly believed in the service charge and sold each business man individually on the idea.

Bank 27.—Many small accounts closed out entirely, reducing a considerable amount of work. Transferring checking accounts to savings accounts, building up checking accounts, and a revenue derived from the service charge.

Bank 28.—We believe the service charge on checking accounts will be a uniform practice in all banks. It is spreading very rapidly and in our bank it has been a marked success in two years' actual experience.

Bank 29.—We did lose a number of accounts, but their balances were exceedingly small and were a positive loss to the bank. However, we have again reopened a number of these accounts as people realized that they had been getting all the benefits of a checking account at a distinct loss to the bank.

Bank 30.—We put the service charge into effect a year ago last January. The amount of monthly charges has been declining ever since, as customers are slowly building up their balance, and thus escaping the charge. Of course, there will always be some folks who cannot or will not carry the required amount and prefer to pay the service charge rather than be without

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the service as already we have had many cases of reopened accounts in which people have tired of trying to run their own bank and pay by cash. They have found that we, by handling it on a wholesale basis, can do it cheaper than they can themselves individually. At the present time we hear so little complaint that we can almost say there is none; as our educational program set forth and showed that it does cost banks considerable to handle a checking account.

The Service Charge and the Banker.—To the banker, the service charge means:

- (a) Decrease in small checking accounts.
- (b) Increase in total demand deposits.
- (c) Profitable balances.
- (d) Reduction in overdrafts.
- (e) Decrease in overhead costs.
- (f) Source of quick revenue.
- (g) Reduction in interest paid and not earned.
- (h) Education of depositors to bank costs.
- (i) Increased earnings.

Any business lost is usually unprofitable.

The Service Charge and the Depositor.—To the depositor the service charge means:

- (a) A new appreciation of the value of checking account service.
- (b) Education as to bank costs.

- (c) A disposition to be fair.
- (d) Better service from his bank.
- (e) Appreciation of the value of a substantial balance which:
 - (1) Builds his credit.
 - (2) Meets his emergencies.
 - (3) Creates confidence in him.
 - (4) Earns prestige for him.

The Service Charge and the Public.—To the public, the service charge means:

- (a) Stronger banks through increases in deposits and earnings.
- (b) More education and a knowledge of the banking profession.

Conclusion.—The service charge on demand deposits, as a remedy for unprofitable checking accounts, at least deserves the consideration of every banker. The facts herein presented indicate a strong case for the proposition. Many banks have already installed the charge and it is producing the desired results and it will only be a few years before the service charge on demand deposits will become a uniform practice among banks throughout the country.

APPENDICES

APPENDICES

APPENDIX I

Geographical Distribution of Replies from Questionnaire

California—	Indianapolis
Los Angeles	LaFayette
Connecticut—	Muncie
Hartford	Kentucky—
New Haven	Louisville
Georgia—	Maine—
Atlanta	Bangor
Illinois—	Maryland—
Champaign	Baltimore
Chicago	Massachusetts—
Danville	Boston
Decatur	Springfield
DeKalb	Michigan—
Mattoon	Flint
Moline	Grand Rapids
Morris	Royal Oak
Peru	Ypsilanti
Rock Island	Minnesota—
Savanna	Minneapolis
Indiana—	Missouri—
Evansville	Kansas City
Gary	St. Louis
Greencastle	

New York—	Pennsylvania—
Jamestown	Butler
New York City	Franklin
Syracuse	Hazleton
Utica	Philadelphia
Westfield	Pittsburgh
Ohio—	Virginia—
Akron	Richmond
Barberton	Washington—
Cleveland	Tacoma
Columbus	Wisconsin—
Dayton	Beloit
Marion	Fon du Lac
Springfield	Janesville
Steubenville	Madison
	Ripon

RESULTS OF QUESTIONNAIRE

A questionnaire was distributed among 100 banks in various parts of the country, as a result of which 71 replies were received.

The purpose of the questions was to find out how the service charge was working in actual practice, methods used in installing and operating it, the opinions of those who have had experience with it as to its merits or demerits, and just how much it has accomplished for those who have used it.

Question I

The banks do not want to make any exceptions to the rule. They want to collect the charge from every one who should rightfully pay it.

While they realize that a certain number of people will withdraw their accounts, they are anxious to retain as many as possible of their present customers, provided they can retain them on a profitable basis.

As far as it is possible, they want to build the balances of the depositors affected.

From your experience, do you consider these three things possible?

ANSWERS

Yes	55
Qualified Yes	13
Qualified No	0
No	3
	<hr/>
	71

Qualified answers and comments include:

1. Some exceptions are necessary.
2. We make no exceptions in regard to service charge on our commercial accounts. We are, of course, anxious to retain all the customers we can and hope those who remain with us will build up their balances so they will be profitable to the bank.

3. Some exceptions are necessary, such as:

- (a) Small accounts that are directly related to other good accounts.
- (b) Accounts of religious and fraternal organizations.

It is merely a question of salesmanship. Most people see the justice of the bank's attitude and either:

- (a) Cheerfully submit to the charge.
- (b) Build up their balances or
- (c) Transfer to a savings account not subject to check.

Naturally, the banks would much prefer not to have to make the charge and would rather see the balances increased to a point where the accounts would be profitable. The successful application of the service charge on the above basis is not only possible, but quite easy if handled in the right way.

4. Yes, with the exception of the first rule. Exceptions are usually made because of affiliated accounts, bond business, etc.

5. Yes, in the main.

6. Accounts lost here were only ones unprofitable and mostly those that had never been profitable.

7. Only exception is church accounts.

Collect from all others.

We tried to retain all accounts possible.

A considerable number have increased the balances and are not now subject to the charge.

8. No exceptions except cases controlled by courts which are very, very few.

9. Increasing balances is the chief purpose and not the small amount received from charges.

10. Not only possible but practical.

11. We make absolutely no exceptions. No desirable accounts lost and average balances have increased.

12. Yes, all three are possible, as we know from experience.

13. These three principles can be carried out to a considerable extent.

14. The service charge will cover the cost of carrying the account, but is not profitable and we would prefer to

have the customer build up the account to a profitable basis.

15. We do make exceptions to the rule. It is our object to collect the service charge from every one who should pay it, but I am sure our experience is not unlike the experience of other banks in that occasionally an officer of a firm carrying a good account, or some one who is unusually active in securing new business for the bank, will want to carry a checking account with an average balance under our regular requirement. Such exceptions are not made promiscuously, but it is obvious that some exceptions in unusual circumstances must be allowed.

It is true that a certain number of people withdraw their accounts because of the service charge, but we should say that such withdrawals are usually by people who do not have a sufficient amount of money available to keep their average up to our requirement and who have no near prospects of increasing their supply of cash on hand, or whose present need for checking account service is so small that it does not justify the expenditure of the service charge. In common with other banks, we want to keep as many of our present customers as possible, provided their accounts are profitable, or at least do not show a loss.

It seems improbable that the system of making a flat service charge when average balances fall below a specified minimum is in itself conducive to the building up of business by the depositor affected.

16. No. For example, we have a customer who carried a profitable account and his wife wishes to carry a household account, which from our experience is liable to be overdrawn from time to time; we still do not feel that we can

apply a charge to such an account. The same holds true of officers of corporations carrying large balances and occasionally we are forced to carry accounts of near relatives of good customers.

17. From our experience with the service charge, we consider it possible for a bank to charge all its customers, without making any exception to the rule. It must be realized that some accounts will be lost. However, if the service charge is properly sold to the customer, little trouble will be experienced. This is best done by showing them an analysis of their account and explaining to them just how they may overcome the service charge by building up their balances, drawing less checks, etc. We feel that it is possible to retain practically all depositors who have been handled in this manner. Our experience is that many of our customers have built up their balances and they are proud of the fact that they are showing the bank a profit instead of a loss.

18. We make a number of exceptions for business reasons, but the number is very limited in comparison with total number of accounts.

19. We heartily recommend that the service charge should be installed with no exceptions to the rule. Experience of banks installing it with exceptions results in the exceptions becoming the ruling.

Our experience from the first year's operations which started March, 1927, was as follows:

36% of accounts treated pay the charge
38% of accounts build up their balances
26% of accounts were closed

Sixty per cent of the accounts closed carried balances ranging from \$25 down to \$1.00 or less. These were accounts which always kept the activity of the teller's windows and the bookkeeping department at a high point.

20. We do not make any exceptions to the service charge rule and we do collect the charge on customer's balances that are not commensurate. We have had a few of our accounts withdrawn due to the fact of the charge, but such accounts were not handled on a profitable basis. We make it a rule to urge upon our depositors the necessity for them to keep balances of \$100 or more in order not to be charged.

21. The first statement as to collecting the charge from every one who should rightfully pay it, has been found impracticable with us. We make exceptions due to business connections, amount of business with other departments, etc. The second and third statements, however, are quite true.

22. This bank does not make any exception to the rule of making service charges. It has been our experience that the service charge properly handled and explained does not meet with any great amount of opposition, as people realize that they must pay for what they receive, and if they are not carrying sufficient balance to enable the bank to handle their account on a profitable basis, they do not object if a service charge is made.

23. In the event that a depositor carries a very good balance in an interest account, we make an exception. This happens very frequently.

The percentage of accounts closed because of service charges is very small.

This bank would prefer to be obliged to make no service

charges whatever providing the depositors in this particular class of accounts would build up their balances to the required amount.

24. These three things are possible. We have lost comparatively few accounts and none that we would consider worth while.

25. We believe these three things possible to a very high degree. Of course, they can never all be followed without exception.

Question II

About what percentage of your checking accounts are profitable?

ANSWERS

A limited number of banks answered this question. These are tabulated as follows:

Bank	Percentage of Profitable Accounts	Bank	Percentage of Profitable Accounts
No. 1	25	19	75
2	51	20	65
3	25	21	80
4	35	22	50
5	93	23	90
6	85	24	50
7	80	25	50
8	90	26	40
9	42	27	35
10	100	28	66
11	50	29	20
12	50	30	75
13	60	31	20
14	60	32	60
15	15	33	40
16	50	34	90
17	68	35	50
18	75	36	50

Percentage of Profitable Accounts		Percentage of Profitable Accounts	
Bank		Bank	
37	36	44	33
38	100	45	40
39	80	46	50
40	50	47	75
41	55	48	33
42	25	49	40
43	90	Median 53.4%	

Other qualified answers and comments include:

1. Very high.
2. All above \$300 average daily balance.
3. Practically all.
4. Since applying the service charge our unprofitable accounts have been greatly reduced.
5. Third unprofitable, third just about pay their way, and third are profitable.
6. All, since we are making service charge.
7. 60 per cent before adopting service charge.
8. About 30 per cent were before service charge was started. About 68 per cent now profitable.
9. About 75 per cent now. Before charge—50 per cent.
10. 35 per cent prior to installation of service charge.
11. 80 per cent. Before service charge not over 50 per cent and likely less.
12. Practically all now (after charge) carry themselves.
13. 64 per cent of commercial accounts were under \$100, amounting to 3.6 per cent of total deposits.
14. Unknown exactly, but materially increased since our service charge campaign.
15. Practically 100 per cent because those with less than the required minimum pay the charge for service.

16. Before service charge, 40 per cent; since charge, 80 per cent.

17. About 22 per cent of our checking accounts are unprofitable; 53 per cent show neither profit nor loss; and 25 per cent are profitable.

18. We are analyzing approximately five hundred business accounts in this bank, and find that 49 per cent of them are on a charge basis, the charges running all the way from 30¢ to \$30 or \$40. On our personal checking accounts we are charging approximately 225 out of 1662 accounts.

19. About 65 per cent of all the individual checking accounts were below \$100 prior to the charge and had an average daily balance of less than \$25. These same accounts represented only 6½ per cent of the total deposits.

Question III

Do you consider educational work concerning the service charge advisable?

ANSWERS

Yes	61
Qualified Yes	4
Qualified No	1
No	5
	<hr/>
	71

Qualified answers and comments include:

1. Yes, but would prefer a joint educational advertising campaign over the signatures of all local banks.

2. Educational work concerning the service charge is certainly advisable. The success of our campaign, we feel sure, was due to the educational work conducted before it

was put into effect, not only among the depositors, but also with the clerks, officers, and directors.

3. Some sort of propaganda (I use the word advisedly) must be resorted to, to offset the thorough advertisement made by banks a few years back to the effect that people should "pay their bills by check." It seems to-day that that advertising was over-effective.

4. I consider educational work concerning the service charge very advisable. Of course, the best method would be to have all of the banks in a city do this under a clearing house agreement, but if it could not be so done, then the individual bank instituting the charge must do so alone.

5. Education of the customer is absolutely essential if the service charge is to be a success. When the service charge was inaugurated in this bank we tried to get in touch with all our business accounts in order that we might go over the analysis of the account with them for several months past and explain the various set-ups, and sell them on the idea that the account should show the bank a profit.

6. We consider the educational work concerning the service charge the keynote and attribute it to the success of the plan.

7. We have endeavored to educate our customers by sending out a form circular regarding the service charge and assuring them that we are in business to make money and cannot afford to let their accounts show a loss.

8. The only educational work which we did concerning the service charge is the preparation of a booklet which is sent out with the notice of the charge. We have thought it more advisable to make the service charge to the customer's

account, notifying him and at the same time inviting him in to talk it over, more in detail, with one of our officers. After going over it with the customer, we may refund the charge—if the first time—upon his promise to maintain a larger balance.

9. Educational work concerning service charges, where they have not been previously introduced, is absolutely necessary. It is also necessary, I believe, that all banks in a community work together on a matter of this kind.

10. I do not advise general broadcasting on the subject, as it is desirable to reach only those customers affected. General distribution of literature, newspaper advertisements are bad because they are liable to offend many people who would never be affected by the charge.

11. We most earnestly recommend educational work to prepare bank's customers for the service charge.

12. In our case, not necessary, as the clearing house association has established a uniform charge.

13. Advisable, but difficult to get over.

14. Yes, very necessary. It's hazardous to install it without educational work.

15. Absolutely necessary.

16. Yes, we utilized three months' campaign of education before adopting the charge.

17. Cannot be done any other way.

18. Extremely so. This is the most important part of the campaign.

Question IV

Would you consider preparing educational work on the charge yourselves?

ANSWERS

Yes	23
Qualified Yes	6
Qualified No	6
No	36
	<hr/>
	71

Qualified answers and comments include:

1. We send a form letter to customers at the time their accounts become subject to our service charge. This constitutes the extent of our educational work and of course the letter was prepared by us.

2. When we instituted the charge we prepared our own educational work. We started off by requesting the customer to call at the bank in order that we might talk with him regarding his balances and showed him the actual figures and how we arrived at our cost and what it was costing us to carry his account and told him that either a service charge of \$1.00 would be made or a balance of \$200 would be required. Later, due to the slowness of this method we prepared and sent out over a period of nine weeks, circulars leading up to the fact that a charge would be made and the final or ninth circular was only sent to such customers as were to be charged, the others going to all customers.

3. It would be rather hard for the average man to prepare educational matter to sell the public on service charges for personal checking accounts. This was all handled for this bank by a firm that specializes in selling the service charge to the public. Business accounts should be handled individually and personally by the officers of the bank.

4. By no means, no.

5. This will vary according to the set-up of each individual bank. Banks having extensive advertising departments and a personnel with time to devote to preparing such work would be advisable.

6. We would prepare a form letter to be mailed to each of the customers subject to the charge. The letter should explain how a bank makes its profits and should point out that a checking account should have sufficient balance to offset the cost of handling. It should then express the hope that the balance can be built up so that a charge will not be necessary. Finally, it should say that otherwise it will be necessary to make a charge at the end of the *following* month. In other words, give them a month's notice and also invite them to drop in and talk it over with an officer or designated employee. After the sending of the letter, no further notice or advice is necessary, the monthly charge ticket being returned to the customer with his statement and canceled vouchers at the end of the month.

7. If the bank has a good copy-writer, yes. If not, no.

8. We endeavor to have a personal discussion with small depositors.

9. Only in the sense of an occasional folder or circular.

10. Yes, if not otherwise available.

11. We considered it for some time, but finally decided to employ outside help.

12. That should be prepared by financial advertising counsel who have a service tried many times in different types of communities and proven successful.

13. We did consider it but, all things considered, we decided to buy it.

14. No, not if good specialists were available.

15. We did not do the work ourselves and are much pleased with results.

16. No. We believe it is best and we found it so, to hire some competent advertising firm to put on the work systematically.

17. Yes, as communities differ.

Questions V and VI

Would you employ outside help? If so, whom? Financial advertisers?

ANSWERS

Yes	38
Qualified Yes	3
Qualified No	0
No	30
	<hr/>
	71

Qualified answers and comments include:

1. We did employ outside help and have been very glad we did. The work of the firm we employed was very effective and well arranged. The personnel of the firm was fine and it seemed to produce the desired effect.

2. We use our own publicity department.

3. Yes, some good financial advertising firm which makes a specialty of selling the service charge to the public.

4. We used a specialist firm. They are very good.

5. We believe outside help, particularly financial advertisers having studied this plan, should be employed.

6. No. Quite unnecessary.

7. Concerns who have had experience in installing service charge systems.

8. Yes, we did so. The fees, including advertising and

complete installation, were paid in full by the first three months' service charges.

9. We did and would again if it were done over.

10. No, because we have necessary staff.

11. No. The bank should best be able to reach its own customers.

12. Yes. We would employ financial advertisers because they have the proper stuff at hand to meet any situation.

13. Any one who is equipped and has made a study of this work.

Question VII

Do you think it worth while to train employees to handle any objections that may arise?

ANSWERS

Yes	58
Qualified Yes	6
Qualified No	0
No.	7
	<hr/>
	71

Qualified answers and comments include:

1. No. Preferring all objections and inquiries sent to a junior official.

2. That was part of the education campaign to have literature prepared and instruct our people as to how to handle objections.

3. Our counter men, both officers and employees, understand and meet objections which arise.

4. It is decidedly advisable to have employees who are able to handle any objection that may arise, but we do not put them through any special training for the purpose,

relying upon their knowledge of this and related subjects acquired by practical experience.

5. I think it quite important that the employees should be trained to handle any objections that might arise and thoroughly understand our method of cost figuring and our reason for making the charge.

6. Employees should not only be trained to handle all objections that may arise, and there will be a great number of them, but they should be sold on the service charge also in order that they may sell the customers more effectively.

7. Yes. Even though they might not handle difficult objections, it gives them an insight as to what is going on and has good moral effect.

8. By all means, employees of banks should be trained to handle any objections that may arise. A series of meetings with all the employees of every bank in this town was held and the whole proposition was laid before them, showing them in detail the cost of serving these accounts. They were instructed on how to meet the customers' objections and how to sell or convince the customers that the action was justified. This part of the program, we believe, to be very important and should never be overlooked in the installation of the service charge.

9. We do think it necessary to train our employees to be able to answer any objections that may arise. If a customer cannot be satisfied by the explanation that the employee is able to make, then the former is referred to an officer.

10. All employees coming in contact with the public should, of course, be conversant with the details of the

charge, although we do not encourage (in fact, we naturally discourage) a teller from going over the analysis with a customer, because his time is not available for that kind of work.

11. The employees attended two meetings and were instructed on how to handle the objections and were also advised to refer the "hard boiled" ones to an officer.

12. No. All objections are taken care of by some officer of the bank.

13. In a large banking office—yes. In a small bank, any officer should be able to handle.

14. To a limited extent.

15. Employees, such as department heads, should be trained to aid officers in meeting any objections that may arise.

16. Better to refer to officer.

17. Very essential.

18. Yes, very important. Tellers, clerks, and bookkeepers are a bank's point of contact with customers.

19. Yes, sir.

20. Certainly.

21. Of course.

22. The executive officers should handle this detail, as they are advised what to say through their connection with the organization putting on the campaign.

23. Absolutely.

24. This is an important and essential feature; we attribute a good part of our success in our campaign to the informed and wholehearted help of our staff in handling objections.

25. Very much worth while. We conducted classes covering every possible objection.

Question VIII

What is the amount and basis of your charge? (See chart)

SCHEDULE OF SERVICE CHARGES¹

(Study based on 58 towns and cities in 18 states)

(Population as shown in 1920 census)

Amount of charge per month	Basis of charge average daily balance	Number of towns using amount and basis as shown in columns 1 & 2
Towns under 5,000		
50¢	\$ 75	1
50¢	50	1
50¢	100	3
Towns—5,000 to 20,000		
50¢	\$100	6
50¢	50	1
50¢	25	1
\$1	50	1
Towns—20,000 to 50,000		
\$1	\$100	3
\$1	50	1
50¢	100	7
75¢	100	1
50¢	150	1
50¢	75	1
Towns—50,000 to 100,000		
50¢	\$100	5
\$1 allowing 15 checks graduated scale	100	1

¹ All charges are on a monthly basis.

Appendices

Towns—100,000 to 500,000

\$1	\$200	2
\$1	100	4
50¢	100	6
50¢	200	1

On balances under \$100, 50¢ or \$1 according to activity. Balances \$100 to \$200, 20 checks allowed and over that according to activity.

Towns—500,000 or more

50¢	\$100	1
\$1	100	2
\$1	300	1
\$1	500	1

Loss to bank plus a reasonable profit

\$1	\$200	2
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Expense estimated at 3¢ per item

\$2	\$500	1
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Question IX

Would you make any change in the amount and basis of your charge if you were doing it over again?

ANSWERS

No	54.9%
Would Increase	35
Change for Other Reason	10.1

Comments include:

1. We feel that the time will come when this basis will change (50¢ under \$100), as many accounts are still quite unprofitable, depending on the number of checks deposited and the number of checks drawn during the month.

2. When the charge was inaugurated, we made a flat charge of 4¢ per item on checks both deposited and paid. This has recently been changed. We now charge 2½¢ on checks deposited and 4¢ on checks paid.

3. We would increase the service charge from 50¢ to \$1.00.

4. The charge thus far has worked very successfully indeed, and we know of no plan whereby we could change this article or improve on it.

5. We are well satisfied with the present basis of our service charge.

6. Nothing to prevent making a change at any time, but it is usually desirable for all the banks in one place to agree to make the change at the same time. In cities, this is arranged through the clearing house.

7. Yes—raise the amount—but present figure is a clearing house regulation.

8. It is working very satisfactorily. Have had six months' experience only, perhaps not enough to know whether we shall make any change in the rate later.

9. No—although a charge of \$1.00 is necessary to break even, our bankers seem satisfied with 50¢ charge.

10. No. However, after the charge is installed, it might be advisable to increase the charge at the end of the first year's use of it.

11. Yes. Would make no exceptions. Commercial account should stand on its own. What is made on \$300 savings is lost many times on small checking accounts.

12. Would allow maximum of three or four checks without charge.

13. Checking at different times has shown the rate to be right.

14. We would probably raise both the fee and the minimum deposit provisions.

Question X

Do you exempt employees, religious and fraternal organizations from the charge?

Yes	43.6%
No	33.8%

Limited answers include:

Exempt religious organizations only.....	4
Exempt employees only	5
Exempt religious and fraternal organizations.....	5
Exempt employees and religious organizations.....	2
	<hr/>
	16

Comments include:

1. The rule is used here without exceptions. Employees, religious and fraternal organizations are all subject to the charge. Many of the fraternal organizations have consolidated several accounts into one, which now makes them profitable.

2. Certain welfare organizations, wives of business men, who also have accounts with us and the like, are exempt.

3. We do not make these exemptions from the charge, but feel that this was a mistake. The service charge is hard enough to put across in the first place without building up the animosity of religious and fraternal organizations.

4. We do not exempt employees. The only exemptions made being to accounts of religious organizations, accounts which are maintained from collection of taxes; such as city, town, and village treasuries, and charitable organizations.

5. Employees are not permitted to carry checking accounts with other banks, so of course there is no service

charge on such accounts when they are carried here. There are a number of other exceptions made for business reasons, but the number is very limited in comparison with the total number of accounts.

6. I am sorry to say that we do not exempt employees, religious and fraternal organizations from the service charge, but usually these accounts show a small margin of profit.

7. We except religious, fraternal, labor, and charitable organizations. The employees of the banks are not excepted, for the reason that many of our customers would know about it.

8. We make an exemption from this charge in favor of any charitable organizations. As regards employees, we do not permit our employees to carry checking accounts here. To enable them to carry an account without a charge, we have reciprocal agreements with several other banks in this city, whereby they carry our employees' accounts without charge and we do likewise for their employees.

9. Generally, because of affiliated business.

10. No, you cannot make exceptions.

11. The six banks here make no exemptions whatever—all of these three are charged.

12. Only exceptions are employees and accounts showing no activity.

13. We should not.

14. Absolutely *no* exemptions of any kind.

15. All officers and employees comply with the rule.

16. Strictly—no exceptions.

APPENDIX II

Terminology

1. *Service Charge*.—A payment exacted by a bank, from a depositor, either as payment for services rendered or as a means toward increased balances.

2. *Demand Deposits*.—Those handled by the commercial department, against which checks may be drawn.

3. *Average Daily Balance*.—Balance at the close of each day for a month, totaled and divided by the number of days in the month.

4. *Substantial Balance*.—A balance which will enable the bank to pay for the handling of the account and realize a reasonable profit thereon.

5. *Activity Cost*.—A per item cost relative to the handling of checks.

6. *Size Cost*.—Proportional to the total commercial department expense as the amount on deposit bears to the total commercial deposits.

7. *Maintenance Cost*.—Cost of maintaining the account on the books of the bank.

8. *Analysis of an Account*.—A method by which an account is determined to be profitable or unprofitable.

9. *Time Deposits*.—Those handled by the savings department and not subject to check.

10. *Reserve*.—A percentage of deposits kept uninvested for emergency.

11. *Float*.—Amount of funds in the process of collection.
12. *Outstanding Item*.—One that has not yet been collected.
13. *Daily Ledger Balance*.—Balance at the close of each day, after all deposits and checks have been entered.
14. *Loanable Balance*.—That portion of the daily average balance subject to earnings, deductions for float and reserve having been made.
15. *Minimum Balance*.—That balance set by analysis, below which an account cannot drop without being unprofitable.

APPENDIX III

TABLE 1

ORIGINAL INVESTIGATION CONDUCTED BY ILLINOIS BANKERS'
ASSOCIATION

COOK COUNTY INCLUDING CITY OF CHICAGO

<i>Pctg. of Accounts</i>	<i>Under</i>	<i>Average</i>	<i>Pctg. of Deposits</i>
11.00%	\$ 25.00	\$10.99 represent	.0015%
19.60	50.00	21.76 "	.053
30.00	100.00	39.78 "	.149
47.50	200.00	78.27 "	.46
60.00	300.00	109.00 "	.81

40% of the accounts carry 99.19% of the money

STATE OF ILLINOIS NOT INCLUDING COOK COUNTY

34.07%	\$ 25.00	\$ 7.08 represent	1.06%
49.08	50.00	14.42 "	3.11
63.92	100.00	23.50 "	6.61
75.35	200.00	41.25 "	13.85
81.90	300.00	59.18 "	21.43

Accounts between \$100-\$200 average \$144.00

Accounts between \$200-\$300 average \$262.91

36.08% of the accounts carry 93.39% of the money

ALL BANKS IN ILLINOIS

29.2%	\$ 25.00	\$ 7.37 represent	.62%
42.9	50.00	15.13 "	1.82
56.8	100.00	25.32 "	4.02
69.5	200.00	47.03 "	9.32
77.2	300.00	64.92 "	14.92

22.8% of the accounts carry 85.1% of the money

NOTE—These divisions were made because of the metropolitan character of banking in the City of Chicago where a large portion

of the banks have for many years required a minimum balance although up to the time the survey was made very few charged their customers on minimum balances.

Cook County, including Chicago (Chicago being the predominating factor in Cook County), was segregated from the rest of the State because of the fact that it was suspected at the time of the survey that individual balances in the suburban towns surrounding Chicago would average higher than in the rest of the State.

It is quite interesting to note that since this survey was made in Illinois other surveys have been made throughout the country and individually by banks that were interested in their own institutions, the results in almost every instance conforming very closely to the results of this original survey.

TABLE 2¹
INCOME CHART, 30 DAYS, 5%

<i>Average Daily Balance</i>	<i>Income on Full Balance</i>	<i>Income Less 10% Reserve</i>	<i>Income Less 15% Reserve</i>
\$1,000,000.00	\$4,166.67	\$3,750.00	\$3,541.67
500,000.00	2,083.33	1,875.00	1,770.84
400,000.00	1,666.67	1,500.00	1,416.68
300,000.00	1,250.00	1,125.00	1,062.51
200,000.00	833.33	750.00	708.34
100,000.00	416.67	375.00	354.17
90,000.00	375.00	337.50	318.74
80,000.00	333.33	300.00	283.32
70,000.00	291.67	262.50	247.90
60,000.00	250.00	225.00	212.48
50,000.00	208.33	187.50	177.06
40,000.00	166.67	150.00	141.85
30,000.00	125.00	112.50	106.23
20,000.00	83.33	75.00	70.82
10,000.00	41.67	37.50	35.42
9,000.00	37.50	33.75	31.87
8,000.00	33.33	30.00	28.33
7,000.00	29.17	26.25	24.79
6,000.00	25.00	22.50	21.25
5,000.00	20.83	18.75	17.71
4,000.00	16.67	15.00	14.17
3,000.00	12.50	11.25	10.63
2,000.00	8.33	7.50	7.08
1,000.00	4.17	3.75	3.54
900.00	3.75	3.38	3.19
800.00	3.33	3.00	2.83
700.00	2.92	2.63	2.48
600.00	2.50	2.25	2.12
500.00	2.08	1.88	1.77
400.00	1.67	1.50	1.42
300.00	1.25	1.13	1.06
200.00	.83	.75	.71
100.00	.42	.38	.35
50.00	.21	.19	.18

¹ *Does the Account Pay?*—Bulletin issued by American Bankers' Association.

TABLE 3

FEDERAL RESERVE BANK OF NEW YORK Schedule Showing When the Proceeds of Items Will Become Available

(Superseding Schedule Issued March 1, 1927 as revised to April 15, 1928)

IMMEDIATE CREDIT

When received by 9 a.m.
New York Clearing House banks (Reference to List A, page 4)
Other New York City and Brooklyn banks (Reference to List B, pages 6 and 7)
Northern New Jersey Clearing House banks (Reference to List C, page 8)
Checks and warrants on Treasurer of the United States, Washington, D. C.
When received by 3 p.m. (Saturdays 1 p.m.)
Checks on Federal Reserve Bank of New York and Buffalo Branch
Officers' checks of other Federal Reserve Banks
Federal Reserve Exchange Drafts
Federal Reserve Transfer Drafts

Districts		
No.		No.
1	Chicago	7
2	St. Louis	8
3	Minneapolis	9
4	Kansas City, Mo.	10
5	Dallas	11
6	San Francisco	12

Federal Reserve Cities and Federal Reserve Branch Cities in this column			Localities outside of Federal Reserve Cities and Federal Reserve Branch Cities in this column		
One Calendar Day After Receipt			CLOSING TIME FOR DEFERRED ITEMS		
New York City—Checks and items on institutions not mentioned above, which the Federal Reserve Bank of New York may elect to handle, when received by 9 a.m.			Payable in Second District		
			3:30 p.m. Saturdays 1 p.m.		
			Items \$400 and over 3:30 p.m. Saturdays 1 p.m.		
			Payable in other Federal Reserve Districts		
			12:30 p.m. Saturdays 12:30 p.m.		
			Items \$100 and over 3:30 p.m. Saturdays 1 p.m.		
Two Calendar Days After Receipt			Two Business Days After Receipt		
Cleveland District 4			Banks in		
Cincinnati Branch of 4			Connecticut **New Jersey		
Charlotte Branch of 5			Delaware **New York		
Atlanta District 6			District of Columbia *Pennsylvania		
Birmingham Branch of 6			Maine Rhode Island		
Jacksonville Branch of 6			*Maryland Vermont		
Nashville Branch of 6			*Massachusetts *Virginia		
Chicago District 7			New Hampshire		
Detroit Branch of 7					
St. Louis District 8					
Louisville Branch of 8					
Minneapolis District 9					
St. Paul In District 9					
Three Calendar Days After Receipt					
New Orleans Branch of 6					
Memphis Branch of 8					
Little Rock Branch of 8					
Kansas City, Mo. District 10					
Kansas City, Kans. In District 10					
Omaha Branch of 10					
Oklahoma City Branch of 10					
Dallas District 11					
Four Calendar Days After Receipt			Four Business Days After Receipt		
Helena Branch of 9			Banks in		
Denver Branch of 10			*Georgia *Minnesota		
El Paso Branch of 11			*Illinois *Missouri		
Houston Branch of 11			Indiana *North Carolina		
San Antonio Branch of 11			Iowa *Ohio		
Spokane Branch of 12			*Kansas South Carolina		
Salt Lake City Branch of 12			*Kentucky West Virginia		
Portland, Ore. Branch of 12			*Michigan Wisconsin		
Seattle Branch of 12					
Five Calendar Days After Receipt			Five Business Days After Receipt		
San Francisco District 12			Banks in		
Los Angeles Branch of 12			*Alabama *Nebraska		
			*Arkansas *Oklahoma		
			*Florida *Tennessee		
			Mississippi		
			Seven Business Days After Receipt		
			Banks in		
			Arizona North Dakota		
			*California Oregon		
			*Colorado South Dakota		
			Idaho Texas		
			*Louisiana Utah		
			*Montana *Washington		
			Nevada Wyoming		
			New Mexico		

* Except banks in cities referred to in the first column.

** Except banks in Northern New Jersey Clearing House Association.

TRANSIT (Float) Account of

A. B. J. Corporation

(General Ac)

(over)

Month of

April 19 28

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ANALYSIS OF ACCOUNTS

EXAMPLE 1¹

Account of William Sherwood

1. Average Balance	\$50.00
2. Less Reserve (15%)	7.50
3. Loanable Balance	42.50
4. Interest income (@ 6%)	2.55
5. Expense Cost	
A. Number of Accounts Cost	\$1.77
B. Activity (15 items @ 2½¢)	4.50
C. Overhead (650 accounts)	3.26
TOTAL.....	9.53
NET LOSS \$6.98	

EXAMPLE 2²

THE VENDO COMPANY

Roselle, New York

Analysis of Account for the Month of August

Average daily balance	\$3,110.50
Daily average in process of collection....	\$1,512.00
15% Reserve in vault and with banks..	466.57
	1,978.57
Average balance subject to earnings.....	1,131.93

INCOME

Interest on available balance at 5%.....	\$ 4.71
--	---------

COST

Number of checks—600 at 4¢.....	\$24.00
Special check books furnished.....	3.00

¹ Devlin and Bennett, Inc.—Booklet—*What About the Service Charge?*

² A Service Charge Plan for Progressive Banks—*Bulletin* published by Edward R. Burt & Co., Certified Public Accountants—Chicago, Illinois.

Appendices

OVERHEAD

For size \$3,110.00 at 31¢ per M. per month	.96	
For maintenance at 40¢ per month.....	.40	
		<hr/>
		28.36
LOSS		23.65
		<hr/>
Remarks		

EXAMPLE 3³

NameEXCELSIOR MANUFACTURING COMPANY...
 Month..Aug. 26 to Sept. 25.....1921.

ANALYSIS OF ACCOUNT

SUMMARY

Total of Daily Balances	\$17,273.00
(Divide by days in month	31)
AVERAGE DAILY BALANCE	557.00
One-day Items	\$6,586.....
2 X Two-day items	5,402.....
4 X Four-day items.....	26,204.....
Float One-day Basis	
(Divide by days in month...31)....	38,192.....
AVERAGE DAILY FLOAT	1,232.00
NET {BALANCE	
{OVERDRAFT	675.00
ADD 15%..Reserves	84.00
DEFICIT BALANCE	759.00
LOSS—for month at 6%.....	3.79
Printing checks 9/5/21.....	4.50
Held for Pay Roll 10 Mo. 4 das.....	1.98
Total Loss	10.27
.....	
Have 10M loan 6% due 10/1/21....	

³“Does the Account Pay?”—*Bulletin* issued by American Bankers' Association.

EXAMPLE 4¹

LITTLE NATIONAL BANK

Little, New York

ANALYSIS OF ACCOUNT

.....The Kato Company
From.....August 1.....To..August 31, 1928.....
Average daily balance.....	\$ 3,110.50....
Amount of out of town checks.....	15,120.00....
Daily average of out of town checks.....	504.00....
Number of checks deposited.....	175
Number of checks paid.....	425
Total number of checks.....	600

Average daily balance.....\$ 3,110.50....

Less:

Daily average of out of town checks

\$504.00—3 days to collect.....\$1,512.00....

15% Reserve in vault and with other

banks 466.57.... 1,978.57....

Average balance subject to earnings..... 1,131.93....

INCOME

Interest on available balances \$1,131 @ 5% 1 month 4.71....

Exchange paid 1.35....

6.06....

Charge for activity 600 checks 4 each.....\$24.00

Charge for size \$3,110 x 20 x 1 month's..... .62

Charge for Maintenance 40 x 1 month's..... .40

25.02....

LOSS 18.96....

.....
¹Dopler, C. M.—“Customers Like Service Charge,” *Bulletin*
published by Edward R. Burt & Co., Certified Public Accountants,
Chicago, Illinois.

*Appendices*EXAMPLE 5^a

Name.....X..Corporation.....

Month of.....June.....

ANALYSIS OF ACCOUNT

Average daily balance.....\$12,487

Daily average in process of collection..\$2,257

12% Reserve in vault and with banks.. 1,498 3,745

Average balance subject to earnings..... 8,742

INCOME

Interest on available balance @ 5%....\$8,742..... 36.42....

COST

Number of checks deposited..1,375....

Number of checks paid..... 190....

Total checks @ .04 each.....1,565..... 62.60....

Special check books furnished.....

Overhead:

For size \$12,487 @ .31 per M. per mo.. 3.72....

For maintenance @ .27 per mo..... 27..... 66.59....

PROFIT.....

LOSS 30.17....

Remarks

.....

.....

^a Citizens Trust Company, Utica, N. Y.

APPENDIX IV

FORM I¹

Debit Slip Issued in Triplicate

First National Bank and Trust Company

Anywhere, U. S. A.....19..

We are this day charging your account \$1.00. Same being a service charge applied on accounts less than \$100 to partially cover cost of handling same. Our books show your average daily balance to be under that amount for the month ending.....

TO:
.....
.....

Note.—The original is sent to the customer as notice of the charge, the first duplicate goes through the work to debit the maker, and the final slip remains as the bank's permanent record. One credit slip (crediting the proper income account) may be made for the total of these slips for the day.

¹ A. E. Martell Company, Keene, N. H.

*Appendices*FORM II ²*Announcement Card*

First National Bank and Trust Company
Anywhere, U. S. A.

An analysis of our Commercial accounts for the past three months has just been completed.

We find that we have sustained a loss of \$. in the handling of your account for that period and we are charging this amount to your account to save you the inconvenience of sending your check.

If you desire, we would be pleased to have you call at your convenience, at which time we will be glad to review your account with you.

Very truly yours,

.....

Officer in Charge.

FORM III ³*Request for Officer's Help*

Date.....

M.....

Address..... Telephone.....

I had an opportunity to discuss the service charge with this patron to-day. I impressed him with the fact that this bank would not willingly lose a single depositor. I also

² Central Trust and Savings Company, Market & Fourth Streets, Philadelphia, Penn.

³ Citizens Trust Company, Utica, N. Y.

tried to convince him that the service charge is small for the value received. I feel that he is not entirely convinced and recommend further attention by the proper officer.

Handled by.....

Referred to.....

Action taken.....

.....

Result

FORM IV ⁴

Clearing House Agreement

"Every deposit account subject to check and payable on demand, except savings deposits and deposit accounts of the Government of the United States, Commonwealth of Massachusetts, or the City of Boston, the average monthly collected balance of which is less than \$300 in any month, shall be charged not less than \$1.00 as compensation for services rendered by the member bank in handling the account during such month. Any account against which no checks have been drawn during the month shall be exempt from the charge. In applying this regulation every account shall be treated upon its own basis, and must not be combined with any other account under any condition."

FORM V ⁵

Specimen Letter

Dear Depositor:

In common with every other line of business, the banking business has experienced a heavy increase in operating

⁴ First National Bank of Boston, Massachusetts.

⁵ Harris Trust & Savings Bank, Chicago, Illinois.

costs the last few years, and it has therefore been necessary for us to make an exhaustive analysis of the accounts we are carrying. Our analysis shows that under present banking conditions checking accounts with daily average balances of less than \$300 are handled by us at an actual loss.

Unless the balances in such accounts average substantially more than \$300, we make no direct profit on handling them under existing conditions. For good friends, like yourselves, we are willing to carry such accounts under existing conditions without profit to ourselves, counting upon your business with us increasing as the time goes on and your being able to direct your friends and other valuable business to us.

We believe you will agree with us, however, that a checking account is a convenience of distinct value to the depositor, and that it is only fair to ask the depositor who enjoys the convenience of a checking account to pay his share of the actual expense of the bank in rendering this service. We believe it is a distinct service which the depositor does not expect his bank to render him at an actual loss to itself.

After careful analysis and consideration we have come to the conclusion that the fairest way of distributing the cost of rendering checking account service is to make the customary service charge of \$1.00 per month, beginning February first, 1929, on checking accounts in which the daily balance during the month is less than \$300.

We have heretofore waived any service charge on your account when your balances have been nominal, and we would much prefer not to have to charge you now. In the

circumstances we hope you can arrange to carry average balances of at least \$300, regularly, so that it will not be necessary for us to make this service charge on your account for any month.

We appreciate very much the business with which you have favored us, and we want to continue to be of service to you in every way we can.

If the above plan for a service charge is not entirely clear and satisfactory to you, won't you kindly step into the bank at your early convenience and talk it over with one of our officers, who will be glad to go over it with you.

Very truly yours,

APPENDIX V

Questions and Answers

1. Banks never charged before, why do they do it now?

A. Times have changed. The use of the check has increased. Operating costs have increased. Bankers did not know until recently that so many accounts were being carried at a loss.

2. Should exceptions be made?

A. Only in the case of some other profitable connection, with the retention of goodwill and the possibility of future business in mind.

3. How can a depositor escape the charge?

A. By increasing his balance.

4. Does the banker want to lose the unprofitable accounts?

A. No. He does not want to lose a single account, but wants to retain them on a profitable basis either through the payment of the charge or increased balances, preferably the latter method.

5. Why should banks make a service charge on the larger balances? Are they not compensated by the earnings on the deposits?

A. Small balances is only one reason for the charge, for an account may be unprofitable for some other reason, including float, reserve, small percentage of income, or

excessive costs of handling the items and maintenance of the account.

6. Is it economically sound for banks to carry some accounts at a considerable loss, some without profits, and others at a large percentage of profit?

A. No. All accounts should be carried at a reasonable profit to the bank.

7. Is it a fact that a small percentage of the checking accounts are required to earn an excessive profit so that a much larger percentage can be carried at a loss or without profit?

A. This has been discovered to be the truth in the majority of banks through an analysis of the accounts and is the situation which the service charge has been installed to correct.

8. How should the proper charge be determined?

A. By analysis.

9. Does the analysis of costs have any value to the bank aside from the service charge?

A. Yes. It gives the banker a knowledge of what the leaks and losses are and where they are.

10. Should the analysis of costs be carried into considerable detail in banks with deposits of \$1,000,000, \$5,000,000 and \$20,000,000?

A. The first two—yes. The last—no. Analysis is based on the law of averages and it is not necessary to carry it into much detail in the larger banks.

11. Can one bank make a service charge if its competitors do not?

A. Experience has proven that this can be successfully done.

12. Will the service charge materially reduce the deposits?

A. On the contrary, it will increase the deposits.

13. Will any considerable number of customers leave the bank?

A. No. Only a few accounts will be lost and these will in most cases be of the unprofitable class.

14. About what percentage of checking accounts are profitable?

A. Approximately one-half.

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